

*United States Court of Appeals
for the Second Circuit*



APPELLEE'S BRIEF

75-7100

IN THE

**United States Court of Appeals
For the Second Circuit**

Docket No. 75-7100

WILLIAM H. NOLAN, on behalf of himself and
all others similarly situated,

Plaintiff-Appellant,

v.

RICHARD B. MEYER, CARL ANTENUCCI, STEVE NARKER,
THOMAS WHITE, LESLIE C. KISSICK and MICHAEL N.
SOTTILE, as Administrators and Trustees of the Profit Sharing
Plan for the Employees of Merrill Lynch, Pierce, Fenner & Smith
Incorporated,

Defendant-Appellees.

**ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE
SOUTHERN DISTRICT OF NEW YORK**

BRIEF FOR DEFENDANT-APPELLEES

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IN THE
UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT
Docket No. 75-7100

William H. Nolan, on behalf of himself and
all others similarly situated,

Plaintiff-Appellant,

v.

Richard B. Meyer, Carl Antenucci, Steve Narker,
Thomas White, Leslie C. Kissick and Michael N.
Sottile, as Administrators and Trustees of the
Profit Sharing Plan for the Employees of Merrill
Lynch, Pierce, Fenner & Smith Incorporated,

Defendant-Appellees.

On Appeal from the United States District Court for
the Southern District of New York

BRIEF FOR DEFENDANT-APPELLEES

PRELIMINARY STATEMENT

Plaintiff-Appellant appeals from a final judgment
entered in the United States District Court for the Southern
District of New York, pursuant to an opinion and order of
the Honorable Harold R. Tyler, dated January 16, 1975, which
dismissed this action for lack of jurisdiction.

QUESTION PRESENTED

Did the District Court err in finding that the federal Court lacked subject matter jurisdiction of this action?

STATEMENT OF FACTS

The complaint was filed on August 23, 1974. It alleges that appellant was employed by Merrill Lynch, Pierce, Fenner & Smith Incorporated ("Merrill Lynch") from 1957 until 1968 and that during this period of employment he participated in a non-contributory profit sharing plan for the exclusive benefit of Merrill Lynch's employees (the "Plan") (5a).* The Plan, which was administered by the appellees, was amended in December, 1960 to include the following forfeiture provision:

11.1 A participant who, in the determination of the Committee, voluntarily terminates his employment with the Corporation or provokes his termination and engages in an occupation which is, in the determination of the Committee, competitive with the Corporation, or any affiliate or subsidiary thereof, shall forfeit all rights to any benefits otherwise due or to become due from the Trust Fund with respect to units credited for fiscal years subsequent to the fiscal year ended December 30, 1960 (5a).

The forfeiture provision was operative for a period of six months after an employee's termination of employment. Any units not forfeited during that period were required to be paid to the employee (35a). All forfeited units were reallocated among continuing participants of the Plan (31a).

The suffix "a" as used herein refers to the Appendix. "A. Br." refers to appellant's brief on appeal.

Article 22 of the Plan provided, finally, that:

'The validity of the Plan or any of the provisions thereof shall be determined under and shall be construed according to the laws of the State of New York."

In or about October, 1968, appellant left Merrill Lynch's employ and went to work for a competitor (6a). Units which had accrued to his account prior to December 30, 1960 were paid to him in full (6a). Units which had accrued after that date were forfeited pursuant to the above provision (4a, 6a).

RELATED ACTION IN STATE COURT

Prior to the commencement of this action, a challenge to the validity of the forfeiture provision of the Plan was rejected by the New York State Courts in Smith v. Meyer, 78 Misc.2d 711, 357 N.Y.S.2d 586 (Sup. Ct. N.Y. Co. 1973), aff'd, 44 A.D.2d 778, 355 N.Y.S.2d 314 (1st Dept. 1974), leave to appeal denied, 34 N.Y.2d 517 (1974). Smith was a class action against the appellees herein brought on behalf of a class which included the appellant. The plaintiff was represented by the same attorney who represents the appellant Nolan. The New York Supreme Court granted defendants' motion to dismiss the complaint, holding that the forfeiture provision of the Plan was valid and did not constitute an unreasonable restraint of trade. The Appellate Division affirmed the dismissal, and the Court of Appeals denied leave to appeal.

THIS ACTION

This action was commenced promptly after leave to appeal was denied in Smith. The complaint seeks a declaratory judgment that the forfeiture provision of the Plan is void and unenforceable on the ground that it violates the "common law" and "the legislative intent and public policy considerations" of the Sherman Anti-Trust Act, 15 U.S.C. § 1 et seq.; Subchapter D of the Internal Revenue Code of 1954, 26 U.S.C. § 401 et seq.; and the Welfare and Pension Plans Disclosure Act, 29 U.S.C. § 301 et seq. in that it allegedly constitutes "an unreasonable restraint on competition" (10a-lla). Federal jurisdiction is purportedly based on diversity of citizenship, the alleged existence of a federal question under the above cited statutes, and "upon the common law under the principles of pendent jurisdiction" (2a). Plaintiff did not purport to invoke federal question jurisdiction under 28 U.S.C. §1331, as he now does, on the basis of a spurious "federal common law" of profit sharing plans.

On September 18, 1974, defendants moved to dismiss the complaint for lack of jurisdiction and for failure to state a claim for relief (14a). The Court agreed that inasmuch as the defendant Carl Antenucci, like Nolan, was a citizen of the State of New Jersey, jurisdiction could not be based on diversity of citizenship (57a-58a). That conclusion is not challenged on appeal.

Defendants also pointed out, inter alia, that Nolan's purported claim under the Sherman Anti-Trust Act was time-barred, and could not serve as a basis for federal jurisdiction, inasmuch as the forfeiture had occurred more than four

years prior to the commencement of this action. Appellant agreed that the statute of limitations barred his purported Sherman Act claim. In an effort to "[preserve] a timely Sherman Act claim and diversity jurisdiction" (A Br. 5), however, appellant cross-moved to add a new plaintiff whose purported Sherman Act claim was not time barred, and to drop Mr. Antenucci as a party defendant.

At oral argument on November 8, 1974, appellant withdrew his cross-motion (54a). Having abandoned his claim of diversity jurisdiction and federal question jurisdiction under the Sherman Act, plaintiff then argued, for the first time, that subject matter jurisdiction was based upon "federal common law" (53a-58a). The District Court rejected that argument and dismissed the complaint for lack of jurisdiction. It held that:

Neither the specific statutes cited by plaintiff nor general federal public policy considerations ... support the extension of federal question jurisdiction to cover profit-sharing plans in general or this Plan in particular. (57a)

Judgment dismissing the complaint was entered on January 20, 1975 (59a).

ARGUMENT

POINT I

THERE IS NO "FEDERAL COMMON
LAW" RELATING TO PROFIT SHARING
PLANS WHICH GIVES RISE TO
FEDERAL QUESTION JURISDICTION

Although the complaint attempts to invoke certain federal statutes as a basis for federal question jurisdiction, appellant argues that he does not seek to base jurisdiction, or his claim for relief, upon a federal statute (A.

Br. 19-20). Rather, appellant claims that federal question jurisdiction is based upon a "federal common law" which allegedly came into existence when Congress demonstrated an "over-riding federal concern" with the subject matter of profit sharing plans (A. Br. 6-7). The argument that federal question jurisdiction can be based upon the Congressional "concern" which motivated the enactment of a federal statute, rather than upon the statute itself, is without merit and was properly rejected by the Court below.

The cases relied on by appellant to support the existence of a "federal common law" in this case are clearly inapplicable. All involved direct federal statutory regulation of the subject matter involved, either in the form of federal requirements or prohibitions. For example, in Ivy Broadcasting Co. v. American Tel & Tel. Co., 391 F.2d 486, 490 (2d Cir. 1968), the application of federal common law to telephone rates and service was based on the fact that Congress, through "comprehensive legislation regulating common carriers engaged in interstate telegraph and telephone transmission", had pre-empted state law in that area and had clearly expressed a need for uniform rates and service. Similarly, federal common law was applied to the pollution of interstate waters in Illinois v. Milwaukee, 406 U.S. 91 (1972), since the Constitution and extensive federal regulation in the area precluded the application of state law.

The federal statutes which appellant cites in an attempt to demonstrate the "awesome federal concern" (A. Br. 25) with the subject matter of this action, however, clearly did

not pre-empt state law on the question of the validity of forfeiture provisions of profit sharing plans. The provisions of the Internal Revenue Code relevant to employee benefit plans, 26 U.S.C. § 401 et seq. (1973), seek only to encourage employers, through tax incentives, to establish plans meeting certain standards. *Barlow v. Marriott Corp.*, 328 F.Supp. 624 (D. Mich. 1971); H.R. Rep. No. 93-779, 93d Cong., 2d Sess. 2 (1974). As the Court below held, Section 401 does not prohibit profit sharing plans which do not qualify under its provisions nor does it create a right in the employee to continued qualification of the plan (55a). Accordingly, that statute creates no right of action in appellant and provides no basis for federal question jurisdiction.

Appellant cannot distinguish *Barlow* by arguing that the Court was concerned only with whether there was federal jurisdiction under the statute and not with jurisdiction under the "federal common law" (A. Br. 19-20). If the statute did not create a federal question jurisdiction, then the "concern" of Congress over the subject matter covered by the statute surely cannot be said to have done so. Under appellant's bootstrap reasoning almost every facet of human relations would be pre-empted by "federal common law." For example, the status of marriage results in certain federal tax consequences. According to plaintiff, however, the mere fact that Congress expressed such a concern would mean that marriages should be governed by federal common law rather than state law.

Appellant's claim of federal question jurisdiction is particularly unconvincing, moreover, inasmuch as the "federal common law" which plaintiff claims was violated has nothing to do with the Internal Revenue Code, the policies behind it or with the other federal statutes appellant cites. The only claim appellant makes is that the Plan was unlawful because it "unreasonably restrains competition in interstate commerce" (A. Br. 20). In other words, appellant is attempting to use the Congressional "concern" underlying various federal statutes solely to get in the Courthouse door. Once in, he proposes to conjure up a federal common law of antitrust which he would like to substitute for his defective Sherman Act claim.*

* Even if the statute of limitations did not bar Nolan's spurious Sherman Act claim, the clear weight of authority holds that forfeiture provisions of the sort in question do not violate the federal antitrust laws. See Bradford v. New York Times Co., 501 F.2d 51, 59-60 (2d Cir. 1974); Cullinan v. Merrill Lynch, Pierce, Fenner & Smith Incorporated, No. 72-2046 (7th Cir. April 27, 1973); Rochester Corp. v. Rochester, 450 F.2d 118 (4th Cir. 1971); Austin v. House of Vision, Inc., 404 F.2d 401 (7th Cir. 1969); Graham v. Hudgins, Thompson, Ball and Associates, Inc., 319 F.Supp. 1335 (N.D. Okl. 1970); Mastandrea v. Gurrentz Int'l Corp., CCH Trade Reg. Rep. 1974-2, Trade Cas. ¶ 75,423 (W.D. Pa. Nov. 21, 1974).

It is also clear that an essential element of a violation of Section 1 of the Sherman Act, namely, the existence of a "contract, combination ... or conspiracy in restraint of trade", is completely absent in the case at bar. Nolan at no time entered, or was asked to enter, into an agreement not to compete with Merrill Lynch. There was no contractual limitation of any sort upon his right to seek other employment upon the termination of his employment and, indeed, he in fact was not hampered in finding employment. He commenced working for a competitor immediately upon his termination of employment with Merrill Lynch.

The Welfare and Pension Plans Disclosure Act, as in effect during the existence of the Plan, 29 U.S.C. § 301 et seq. (1973), is also irrelevant to appellant's claim. That Act was intended only "... to secure disclosure and reporting with respect to welfare and pension plans and ... it was not intended to transfer to the federal courts general jurisdiction over the administration of such plans." Lieberman v. Cook, 343 F.Supp. 558, 561-562 (W. D. Pa. 1972). Appellant argues that the Court in Lieberman failed to recognize the "formidable 1958 Congressional declaration of the substantial federal concern with these plans" which he claims did have the effect of transferring to the federal courts general jurisdiction over the administration of such plans (A. Br. 22). This argument is frivolous.

Appellant goes on to argue, in the same vein, that the Pension Act of 1974, 29 U.S.C. §1001 et seq., "... removes any vestige of doubt of federal dominion of the subject matter" of this controversy (A. Br. 26). No claim is made that the forfeiture provision in question would be unlawful under that Act. (Even if it were unlawful, moreover, the Act by its terms does not apply "to any cause of action which arose, or any act or omission which occurred, before January 1, 1975." 29 U.S.C. § 1144 (Supp. 1975).) It is clear that appellant is again attempting to use an irrelevant federal statute for the purpose of concocting a federal anti-trust common law which presumably exists independent of the Sherman Act.

This Court has recently rejected similar attempts to create a federal common law, giving rise to federal question jurisdiction, over pension and profit sharing plans. In Beam v. International Organization of Masters, Mates, and Pilots, No. 74-1725 (2d Cir. February 24, 1975), Slip Op. 1877, the widow of a deceased employee contested the determination by the trustees of a jointly-administered labor-management trust which denied her application for accidental death benefits. The case was before this Court on diversity jurisdiction. This Court found no basis for independent federal question jurisdiction under Section 301 of the Labor Management Relations Act of 1947, 29 U.S.C. §185. Although appellant argued that a federal standard must apply because of "a variety of abuses argued to be unique and endemic in this labor relations field", Beam Slip Op. at 1883, the Court ruled that traditional trust concepts should apply rather than any new federal standard.

In Cuff v. Gleason, No. 74-2504 (2d Cir. April 15, 1975), Slip Op. 2889, this Court, on its own motion, dismissed for lack of federal jurisdiction an appeal involving an allegedly arbitrary application of rules of a jointly-administered pension trust. The Court expressly considered and rejected, as possible sources of federal jurisdiction, each of the following statutes: the Labor Management Relations Act, 29 U.S.C. §186, the Labor-Management Reporting and Disclosure Act of 1959, 29 U.S.C. §501, the

Welfare and Pension Plans Disclosure Act, 29 U.S.C. §308(h) and the Pension Reform Act of 1974, 29 U.S.C. §1001 et seq.

In Haley v. Palatnik, No. 74-1948 (2d Cir. January 24, 1975), Slip Op. 1419, this Court found that the alleged diversion of a payment from an employee education fund to the personal profit of a union official constituted a violation of Section 302 of the Labor Management Relations Act, 29 U.S.C. §186. In so doing, it distinguished the alleged diversion from a "simple breach of fiduciary duty" which would not create federal jurisdiction:

"Where payments are lawfully made in good faith by the employer to the trust fund so that the provisions of §302(c) come into play, the doors of federal court remain shut and breaches of fiduciary duty occurring thereafter are not violations of the old federal law." Haley Slip Op. at 1428. See also 1423.

The Court also observed in a footnote that the Pension Reform Act of 1974 does create a federal cause of action for breach of fiduciary duties, but that Act "does not apply to the conduct involved in this suit because its effectiveness, §414, is subsequent thereto". Haley Slip Op. at 1428, fn.

5.

Appellant argues, finally, that the alleged impact of forfeiture provisions of profit-sharing plans on interstate commerce makes uniform federal common law rules in this area desirable. As authority, appellant quotes excerpts from Merrill Lynch's brief to the Supreme Court in Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Ware, 414 U.S. 117 (1973)

wherein Merrill Lynch argued the need for nationwide uniformity with respect to the validity of the forfeiture provision (A. Br. 29). Appellant, however, completely misses the point of that argument. The point was that the Plan, by its terms, was to be construed and interpreted pursuant to New York law - under which the forfeiture provision was lawful. It was that body of law which it was urged should be uniformly applied. There was no claim made that "federal common law" should be substituted for the law of New York.

Ware is important, however, because the Supreme Court specifically rejected the argument which appellant now puts forth that profit-sharing plans should be judged in accordance with a uniform national standard. Far from holding that a federal common law was applicable, the Supreme Court held that the validity of the forfeiture provision could be decided differently under the laws of different states. Whereas the forfeiture provision had been held to be invalid in California, it was conceded that New York Law was "more permissive." 414 U.S. at 133.

In short, it is clear that no federal statute creates federal subject matter jurisdiction in this case and that vague allusions to "formidable" or "awesome federal concern" do not suffice to create a new federal common law. As this Court recently held in Simon & Flynn, Inc. v. Time Inc., No. 74-1976 (2d Cir. April 2, 1975), Slip Op. 2687, the mere

"aroma" of federal statutory involvement or a "general interest" of Congress in the subject matter of a suit is an insufficient basis for federal question jurisdiction.

POINT II

THE NEW YORK COMMON LAW CLAIMS WERE PROPERLY DISMISSED BELOW

It is well settled that if the federal claims are subject to dismissal under Rule 12(b)(6) then the allegedly "pendent" common law claims should also be dismissed. See United Mine Workers v. Gibbs, 383 U.S. 715, 727 (1966) and Kavit v. A.L. Stamm & Co., 491 F.2d 1176, 1179-80 (2nd Cir. 1974). It has been demonstrated above that plaintiff has asserted no valid federal claim. Accordingly, the allegedly "pendent" New York common law claims were subject to dismissal for lack of jurisdiction in the District Court.

Even if the District Court had jurisdiction over the New York common law claims plaintiff purports to assert, such claims were subject to dismissal under Rule 12(b)(6). Plaintiff in Smith v. Meyer, supra, sued the defendants herein in the State Court on behalf of himself and a class which included the appellant Nolan. The Smith complaint alleged that the forfeiture provision was "void and unenforceable as an unreasonable restraint of trade" under the common and statutory law of New York and the Federal Internal Revenue Code. (22a-23a). The court in dismissing the complaint ruled:

[T]he Courts of this jurisdiction, including the New York State Court of Appeals, have consistently upheld the validity of forfeiture clauses such as provided in Article 11.1 of the Plan. (Kristt v. Whelan, 4 A.D.2d 195, aff'd 5 N.Y.2d 807; Simons v. Freid, 302 N.Y. 323; Kidd v. Oakes, 39 Misc.2d 645; Kerpen v. First Investors Corporation, 45 Misc.2d 793; Matter of Kumm v. Allen, 36 Misc.2d 816; see also Amory H. Bradford v. The New York Times Company, U.S. Dist. Ct., S.D.N.Y., 67 Civ. 3821), and under New York Law where one may choose between working for a competitor of his former employer, and thereby surrender benefits to which he would otherwise be entitled under a non-contributory profit sharing plan, or retaining those benefits by not working for such a competitor, he is not subject to an unreasonable restraint of trade. 357 N.Y.S.2d at 588.

Having been adequately represented in Smith, appellant cannot now relitigate in the federal courts the validity, under New York law, of the same provision of the same profit sharing plan which was upheld in Smith. He is bound by the earlier judgment. See First Congregational Church and Society of Burlington, Iowa v. Evangelical and Reformed Church, 305 F.2d 724 (2d Cir. 1962), cert. denied, 372 U.S. 918 (1963); Graham v. Bd of Supervisors, 25 A.D.2d 250, 269 N.Y.S.2d 477 (4th Dept.), appeal dismissed, 17 N.Y.2d 866, 271 N.Y.S.2d 295 (1966); and Gart v. Cole, 263 F.2d 244 (2d Cir.), cert. denied, 359 U.S. 978 (1959).

Even assuming the District Court had subject matter jurisdiction over the common law claims, and assuming plaintiff were not barred under the doctrine of res judicata from relitigating the validity of the forfeiture provision under New York law, it is clear that the decision in Smith v. Meyer, supra, would be dispositive on New York law and that any purported claim under the common law of New York should be dismissed.

In Bradford v. New York Times Co., supra, this Court was asked to hold a forfeiture provision of an employee benefit plan invalid under New York law. This Court held that the forfeiture provision was valid and enforceable. 501 F.2d at 57. In its recent decision in USAchem, Inc. v. Goldstein, Nos. 74-1201, 74-1223 (2d Cir. February 14, 1975), Slip Op. 1817, this Court was asked to invalidate a forfeiture provision in a profit-sharing plan. Citing Bradford, supra, this Court held that "... the forfeiture constitutes a valid liquidated damages clause which is enforceable." USAchem Slip Op. at 1828.

CONCLUSION

The plaintiff's arguments on appeal are entirely without merit. This appeal is clearly an unjustified attempt to salvage the efforts expended without success in Smith v. Meyer, supra, by asserting the specious afterthought that a newly conceived "federal common law" was applicable. In Simon & Flynn, supra, this Court held that when an unjustified appeal is taken as a "salvage effort" or a "knee-jerk-reaction" to an unfavorable ruling, the judgment appealed from will be affirmed, with double costs awarded to the appellee. That holding is clearly applicable to this appeal.

The judgment of the District Court should be affirmed by this Court, with double costs.

Dated: New York, New York
April 28, 1975

Respectfully submitted,
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